
Country Report

Vietnam

November 2008

Economist Intelligence Unit
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United Kingdom

The Economist Intelligence Unit

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Electronic delivery

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ISSN 1356-403X

Symbols for tables

"n/a" means not available; "--" means not applicable

Printed and distributed by Patersons Dartford, Questor Trade Park, 151 Avery Way, Dartford, Kent DA1 1JS, UK.

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Executive summary

Highlights

November 2008

Outlook for 2009-10

- The ruling Communist Party of Vietnam will keep a tight grip on power in 2009-10, rejecting calls from some quarters (especially groups of overseas Vietnamese) for political pluralism.
- In 2009 and 2010 the fiscal budget will be hit by lower revenue growth, while expenditure will remain high. As a result the budget deficit (excluding on-lending) will widen significantly, to reach the equivalent of 6.8% of GDP.
- As it attempts to avert a major slowdown in the domestic economy, the State Bank of Vietnam (SBV, the central bank) will continue to cut its policy interest rate in 2009. The rate will average 7.3% next year and 5% in 2010.
- The Economist Intelligence Unit expects real GDP growth in Vietnam to fall to 4.3% in 2009 as export growth slows, but it will begin to pick up in 2010, to reach 5.3%.
- Disbursements of foreign direct investment will be severely curtailed by the lack of available financing, which will sharply slow investment growth in 2009-10.
- Global food and fuel prices will ease downwards, and domestic demand is expected to weaken in the forecast period. Consequently, inflation is expected to slow to 8.7% in 2009 and to remain in single digits in 2010.
- We forecast that the current-account deficit will narrow dramatically in the forecast period, to 5.9% of GDP in 2009 and 2.9% in 2010, from an estimated 13.7% in 2008, as a result of a large reduction in the trade deficit.

Monthly review

- Discord has arisen between the prime minister, Nguyen Tan Dung, who wishes to focus on economic growth, and the party's general secretary, Nong Duc Manh, who is more concerned with political and social stability.
- The SBV has reversed its course and has moved to loosen monetary policy. On October 20th it cut its base interest rate from 14% to 13%, and on November 5th the bank reduced the rate further, to 12%.
- The SBV has widened the trading band within which the dong can fluctuate on a daily basis against the US dollar to 3%, from 2% previously.
- Inflation fell by 0.2% month on month in October, signalling an end, at least in the short term, to the increase in inflation that characterised the first three quarters of 2008.
- Since June the monthly trade deficit has narrowed drastically, helping the balance-of-payments position. However, both exports and imports have been contracting since July.

Outlook for 2009-10

Political outlook

Domestic politics The ruling Communist Party of Vietnam will keep a tight grip on power in 2009-10, rejecting calls from some quarters (especially groups of overseas Vietnamese) for political pluralism. There will continue to be small pockets of domestic dissent, but the population has yet to show any appetite for major political change. However, political stability is not assured. The government is currently facing a serious test of its capacity to manage the economy, and there is a risk of demonstrations if economic growth slows sharply. The party is acutely aware that social stability is vital if it wants to maintain full control, and thus it is likely to push ahead with plans for greater spending on social welfare. However, its ability to do this will be constrained by lower revenue growth as GDP growth slows significantly in 2009-10.

The party could also face greater internal strife over the next year or so. The country's current economic problems and the potential for social unrest have weakened the position of the reformist members of the party, including the prime minister, Nguyen Tan Dung, in the eyes of the more conservative members. If the government fails to restore a greater sense of economic stability in 2009, or if the situation deteriorates further, the prime minister could become vulnerable. Mr Dung is already thought to have veered away from the party's traditional ethos of determining policy by consensus, which has upset factions in the 160-member central committee. There appears to be an ongoing rift between Mr Dung, who favours a continued emphasis on rapid economic growth, and the party's general secretary, Nong Duc Manh, who is more concerned with political and social stability. This could lead to conflicting policy responses in reaction to the worsening economic outlook.

The party will continue to use hardline tactics to suppress dissent. Thousands of people reportedly protested in the capital, Hanoi, against the decision by the local authorities to begin redeveloping a site important to the Roman Catholic church. Although the protests have been contained, there are likely to be further such episodes if the party refuses to take a softer approach to dealing with religious and ethnic-minority groups. Another issue that could undermine the party's attempts to maintain a tight grip on power is corruption, given that the leadership continues to be plagued by revelations of graft. The party will need to prove that progress is being made in the fight against corruption to maintain its authority. Ongoing crackdowns on corrupt officials and state-owned enterprises are a good indication that the government takes graft seriously, but they are also a sign of the extent of the problem.

International relations Vietnam's "friends to all" foreign policy is intended to improve the country's economic situation through increased external trade and investment links. The country's eagerness to enter into free-trade negotiations is a strong indication of its dedication to its reform agenda. Given that talks on a free-trade agreement between the Association of South-East Asian Nations (ASEAN) and the EU have

stalled, a representative of the EU's negotiation team announced in mid-October that it might seek deals with individual countries, including Vietnam. This would provide a significant boost to Vietnamese exporters, as the duty on many imports would be likely to fall to zero.

Economic policy outlook

Policy trends The global financial crisis has created new policy challenges for the government. After tightening monetary policy earlier in 2008 to stem inflationary pressures and cool the overheating economy, the government is now facing a situation in which economic growth is set to slow significantly. This requires a change in policy to increase liquidity in the banking sector, and fiscal loosening to counter the negative impact of the slowing external economy. The State Bank of Vietnam (SBV, the central bank) will continue to cut its base interest rate, although the likelihood of lower interest rates significantly boosting growth is low, given the dire outlook for the world economy, including Vietnam's major trading partners. The government will need to focus its efforts on balancing the economy's fundamentals, rather than trying to achieve a GDP growth target (currently 7% in 2009) that in the context of the current outlook for the global economy is unrealistic.

Fiscal policy The budget deficit (excluding on-lending) will widen significantly in 2009-10, to average the equivalent of 6.8% of GDP in 2009 and 6.6% in 2010. Subdued GDP growth in 2009-10 will result in lower revenue growth, but expenditure will remain high, as the government is committed to programmes to improve social welfare provisions. Moreover, the price of oil is expected to decrease considerably in 2009 and remain relatively low in 2010. Oil revenue accounts for around 30% of total government income and a major fall in oil revenue will undoubtedly have a negative impact on the overall budget deficit. The IMF has called on the government to save a significant portion of its "revenue overperformance" from the oil price boom in recent years, but the government instead spent it on improving infrastructure and social development. However, now that the boom appears to be over, the government will not have a kitty of oil funds to fall back on. A reformed personal income tax system (which will give a boost to revenue) will come into effect in January 2009. The new income tax structure will deepen the tax base by making benefits taxable as well as salaries, and will apply the same tax rates to Vietnamese and foreign workers. (The tax threshold for foreign staff will fall to match that for local workers—it is currently twice as high as that for local employees.)

Monetary policy The SBV sharply tightened monetary policy in the first half of 2008 in an attempt to slow credit growth and rein in inflation. However, there has been a major policy reversal since October 20th when the SBV announced its first 100-basis-point interest rate cut. This cut brought the base rate to 13%, and on November 3rd the SBV made a second cut, of another 100 basis points, to reduce the rate to 12%. It has also increased the rate of interest that it pays banks on their compulsory reserves, a move that has in effect lowered the cost of capital for commercial banks. The government is hoping that by cutting its

policy interest rate to raise credit growth, the banking sector will receive a boost, while firms that have become reliant on cheap and easy credit will not have to scale back their activity and face the risk of defaulting on their loan repayment obligations. As it attempts to avert a major slowdown in the domestic economy, the SBV will continue to cut its policy rate in 2009, to average 7.3% in that year and 5% in 2010.

On November 6th the SBV widened the trading band within which the dong is allowed to fluctuate on a daily basis against the US dollar to 3%, from 2% previously. The government hopes that by widening the band it can quicken the managed depreciation of the dong against the dollar, in an attempt to boost Vietnamese exports by making them more competitive. This is a reflection of the government's acknowledgment that the domestic economy is not immune to the consequences of the global financial crisis. However, the extent to which a weaker currency will boost export growth is uncertain at best, given the poor economic outlook for Vietnam's major trading partners.

Economic forecast

International assumptions

International assumptions summary

(% unless otherwise indicated)

	2007	2008	2009	2010
Real GDP growth				
World	4.8	3.6	2.0	3.0
China	11.9	9.6	8.0	7.5
EU27	2.9	1.3	-0.3	0.8
Exchange rates				
¥:US\$	117.8	103.6	97.0	96.0
US\$:€	1.37	1.46	1.29	1.30
SDR:US\$	0.65	0.63	0.67	0.66
Financial indicators				
¥ 3-month Gensaki rate	0.61	0.65	0.60	0.93
US\$ 3-month commercial paper rate	5.06	2.28	2.13	2.79
Commodity prices				
Oil (Brent; US\$/b)	72.7	98.4	65.0	68.3
Gold (US\$/troy oz)	696.7	863.2	707.5	625.0
Food, feedstuffs & beverages (% change in US\$ terms)	30.9	30.2	-26.4	0.8
Industrial raw materials (% change in US\$ terms)	11.2	-1.0	-20.4	-0.5

Note. Regional GDP growth rates weighted using purchasing power parity exchange rates.

The global financial crisis has worsened since mid-September, with record levels of risk aversion and sharp declines in stockmarkets. This has triggered strong action by authorities in the US, the UK, the euro area and elsewhere. Although at least a temporary stabilisation seems likely to be achieved, the crisis has led to a vicious circle of a deteriorating financial environment that is causing severe damage to the real economy, in turn leading to higher defaults and thus further undermining financial conditions. Global GDP growth (in purchasing power parity, or PPP, terms) will slow from 3.6% in 2008 to just 2% in 2009, with only a moderate recovery expected in 2010. The new forecast for 2009 is suggestive of a global recession (usually defined as GDP growth in PPP terms of less than 3%).

Economic growth**Gross domestic product by expenditure**

(D bn at constant 1994 prices where series are indicated; otherwise % change year on year)

	2007 ^a	2008 ^a	2009 ^b	2010 ^b
Private consumption	302,184	313,899	322,580	333,207
	9.6	3.9	2.8	3.3
Public consumption	30,272	31,846	33,438	35,278
	8.9	5.2	5.0	5.5
Gross fixed investment	179,993	206,992	223,137	240,988
	23.0	15.0	7.8	8.0
Final domestic demand	512,449	552,737	579,156	609,473
	13.9	7.9	4.8	5.2
Stockbuilding	19,018	10,200	9,500	9,000
	1.2 ^c	-1.9 ^c	-0.1 ^c	-0.1 ^c
Total domestic demand	531,467	562,937	588,656	618,473
	14.6	5.9	4.6	5.1
Exports of goods & services	449,680	496,774	506,251	524,447
	15.2	10.5	1.9	3.6
Imports of goods & services	498,736	574,666	582,597	600,109
	21.3	15.2	1.4	3.0
Foreign balance	-49,056	-77,892	-76,346	-75,662
	-6.7 ^c	-6.2 ^c	0.3 ^c	0.1 ^c
GDP	461,443^d	489,545	510,710	537,812
	8.5 ^d	6.1	4.3	5.3

^a Economist Intelligence Unit estimates. ^b Economist Intelligence Unit forecasts. ^c Contribution to real GDP growth (as a percentage of real GDP in the previous year). ^d Actual.

The Economist Intelligence Unit expects real GDP growth in Vietnam to fall to 4.3% in 2009, the slowest pace of growth in recent years. Vietnam's economy has already lost momentum in 2008, with real GDP rising by 6.5% year on year in the first three quarters of the year, compared with 8.2% in the year-earlier period. As a result of recessionary conditions in the developed world, most notably in the US, the EU and Japan, which together consume nearly 60% of Vietnam's exports, export growth will slow dramatically in 2009-10. This will have a negative impact on overall economic growth, as exports of goods and services are equivalent to over 80% of GDP (in nominal terms). Although inflation appears to have peaked, households' disposable incomes have been eroded and the rate of private consumption growth will continue to fall in 2009, especially as unemployment rises in line with the slowdown in the domestic economy.

Although foreign investors remain confident about Vietnam's long-term prospects, actual disbursements of foreign direct investment (FDI) will be severely curtailed as a result of a lack of available financing in the forecast period. Liquidity for banks has dried up because banks are refusing to lend to other financial institutions that may not be able to pay back loans (counterparty risk), and because it has become difficult for banks to predict their own liquidity needs. Investment growth will be negatively affected by subdued FDI inflows and by the slowdown in the export sector. Import growth slowed in 2008, and there will be a further fall in growth in 2009-10. This will reflect the weaker domestic economy, the depreciation in the dong and subdued investment-import growth has largely been driven by investment in recent years. Given that growth in exports is forecast to outpace that in imports

in 2009-10, the external balance will make a positive contribution to overall GDP growth.

On the supply side, economic growth will continue to be driven by the industrial sector, although growth in the sector will slow notably in 2009-10. Manufacturing output growth will also wane in the first half of the forecast period, in line with the weakness in external demand. A slowdown in investment and output in both the industrial and manufacturing sectors will temporarily halt the continued deepening of the industrial base. Services growth will also suffer as a result of the global financial crisis and recessionary conditions in many developed countries.

Inflation Consumer price inflation appears to have peaked on a year-on-year basis in August, with the rate slowing in September and October. Nevertheless, inflation remains high, standing at 26.7% year on year in October, with food prices up by around 60%. In monthly terms, though, the slowdown in inflation is much more evident: overall prices declined by 0.2% in October, while food prices fell by 1.9%. The recent loosening of monetary policy could add to inflationary pressures, particularly as the dong is depreciating against the US dollar, making imports more expensive. However, global food and fuel prices are set to fall substantially and domestic demand growth is expected to weaken. This will have a positive impact on inflation, which is expected to slow to 8.7% in 2009. Inflation will stay in single digits in 2010 as external supply-side pressures remain weak.

Exchange rates After acting to control the downward pressure on the dong against the US dollar in mid-2008, the government is now hoping to speed up depreciation to boost export growth. Following a previous widening in May 2008, the SBV has again increased the dong's trading band, this time to "ensure reasonable and stable economic growth". The dong is set to continue to weaken in 2009-10, but there will be a greater degree of volatility given the global financial crisis and the likelihood that the SBV will widen the dong's trading band further. We forecast that the dong will average D17,005:US\$1 in 2009, compared with an estimated D16,548:US\$1 in 2008, and that it will depreciate to D:17,099:US\$1 in 2010.

External sector We forecast that the current-account deficit will narrow dramatically in 2009-10 as a result of a major reduction in the trade deficit. The value of both exports and imports will contract in 2009, in the face of a reduction in demand from Vietnam's leading export markets as well as falling prices for the country's major goods exports. Trends in global crude oil prices suggest that the value of Vietnam's oil exports (the country's largest goods export category) will fall in 2009, before recovering marginally in 2010. The recent sharp widening in the current-account deficit has been driven primarily by soaring imports, many of which have been in the form of capital goods bought by foreign-invested enterprises (FIEs). Owing to the fact that foreign investors will face difficulties acquiring financing in the forecast period, capital goods imports will fall from the high levels of recent years. The slowdown in consumption growth will also curtail growth in imports of consumer goods over the next two years.

In addition to the deficit on the merchandise trade account, the services and income accounts will remain in deficit, although both will narrow significantly in 2009-10. Tourism receipts will decline, but so will imports of trade-related services. The upward trend in the repatriation of foreign investors' income and profits will temporarily reverse in line with the slowdown in the operations of FIEs. Inflows of current transfers will be affected by the slowdown in the US and the EU, which are home to a large number of Vietnamese, and as such we forecast that inflows will fall from the high level reached in 2007. However, the current transfers surplus will still be sufficient to offset the combined deficit on the services and income accounts in 2009-10. We forecast that the current-account deficit will narrow from an estimated 13.7% of GDP in 2008 to 5.9% in 2009 and 2.9% in 2010.

Forecast summary

(% unless otherwise indicated)

	2007 ^a	2008 ^b	2009 ^c	2010 ^c
Real GDP growth	8.5	6.1	4.3	5.3
Industrial production growth	17.0	16.7	7.5	8.8
Gross agricultural production growth	3.4	3.5	3.0	2.0
Consumer price inflation (av)	8.9	24.5	8.7	6.3
Consumer price inflation (year-end)	14.4	20.9	5.1	8.4
Lending rate	11.2	16.1	12.6	10.1
Government balance (% of GDP)	-5.4 ^b	-4.7	-6.8	-6.6
Exports of goods fob (US\$ bn)	48.6	62.0	49.3	55.2
Imports of goods fob (US\$ bn)	58.9	76.6	58.0	61.6
Current-account balance (US\$ bn)	-7.0	-11.6	-5.6	-3.1
Current-account balance (% of GDP)	-9.8	-13.7	-5.9	-2.9
External debt (year-end; US\$ bn)	21.8 ^b	23.2	22.3	23.1
Exchange rate D:US\$ (av)	16,096	16,548	17,005	17,099
Exchange rate D:¥100 (av)	13,666	15,971	17,531	17,812
Exchange rate D:€ (year-end)	23,409	22,016	22,312	22,094
Exchange rate D:SDR (year-end)	25,583	25,735	25,954	25,787

^a Actual. ^b Economist Intelligence Unit estimates. ^c Economist Intelligence Unit forecasts.

Monthly review: November 2008

The political scene

Senior leaders disagree on the economy

In early October the 160-member central committee of the ruling Communist Party of Vietnam held a three-day plenum devoted primarily to discussing the current domestic economic situation and the government's budget for 2009. This was the third plenum to have been held this year—normally there are just two per year—which is a reflection of policymakers' anxiety about the direction of the economy. There has been a divergence between the views held by the prime minister, Nguyen Tan Dung, who favours a continued emphasis on rapid economic growth, and the party's general secretary, Nong Duc Manh, who is more concerned with political and social stability. Judging by the tone of the communiqué issued after the meeting, the more conservative group, centred around Mr Manh, appears to be gaining political ground. The document noted that in 2009 controlling inflationary pressures should remain the top priority, in order to stabilise the domestic economy, while GDP growth should be kept at an appropriate and sustainable rate. At its previous meeting in mid-July, the committee had given the 14-member politburo (the party's executive committee) responsibility for overseeing the economy in 2008, in effect taking the job away from Mr Dung and his cabinet.

However, at a regular cabinet meeting on November 1st, Mr Dung put his own interpretation on the guidance from the central committee by asking ministers to accelerate the implementation of state-funded projects, to prioritise "flexible monetary policy" to control inflation and to maintain relatively strong GDP growth. These are conflicting goals, but it is notable that in late October the State Bank of Vietnam (SBV, the central bank) altered its stance from maintaining a tight monetary policy direction to switching to an expansionary one, which could fuel inflationary pressures.

A journalist is jailed for reporting on corruption

Concerns about maintaining social order have been reflected in the government's efforts to clamp down on the media. On October 15th a court in the capital, Hanoi, sentenced Nguyen Viet Chien, a former journalist on a newspaper, *Thanh Nien*, to two years in prison for "abusing democratic freedoms to infringe upon the rights and interests of the state" and for "tarnishing the images and reputation of the party and state". Mr Chien had reported on the high-profile Project Management Unit No 18 (PMU 18) corruption case, and had been given access to inside information from a number of police investigators. PMU 18, which comes under the Ministry of Transport, became embroiled in controversy in 2006, when its director, Bui Tien Dung, was arrested and accused of embezzling US\$1.8m to gamble on football matches.

Commenting on the case, a Ministry of Foreign Affairs spokesman, Le Dung, said that "the Vietnamese government always encourages the press to take an active part in the fight against corruption in a comprehensive, thorough and lawful manner". Analysts have argued that by arresting Mr Chien, the

government has proved itself to be unwilling to allow the media to operate freely and without interference. Mr Manh has generally taken a hard line towards the media, whereas Mr Dung has adopted a more liberal stance. In early October the latter signed into law a declaration that would require the main ministries to provide “official, prompt, accurate, public and transparent” information about their policies and plans to the local and foreign press. This marks a major step for a government that has historically been cautious about divulging information.

Trial elections for commune-level leaders are considered

The current session of the National Assembly (the legislature) is due to consider a pilot project that would allow the direct election of the chairmen of the commune-level people’s committees. Currently, chairmen are appointed to these positions. This is not the first time that a proposal for local-level democracy has been floated, and it appears that Vietnam intends to follow China’s lead in opening up the political system, albeit slowly and cautiously. However, it is not clear how much public enthusiasm there is for such a move.

Economic policy

The SBV cuts interest rates twice in three weeks

After a period of tightening in the first half of the year, the SBV has reversed its course and loosened monetary policy. On October 20th the SBV cut its base interest rate to 13%, from 14% previously, and on November 5th it reduced it further, to 12%. The SBV noted that the global financial crisis was having a negative impact on the domestic economy. The moves reflected the need to boost liquidity in the market to avert further deterioration in the outlook for domestic growth as the external environment worsens. It is also an indication that the SBV is moving in parallel with other central banks around the world, an encouraging sign given the delayed response to soaring inflation earlier in the year. The SBV will continue to cut rates, especially as inflation abates and the reality of subdued domestic growth in 2009-10 becomes more apparent.

The SBV’s moves to boost liquidity have not been limited to loosening monetary policy. In order to inject liquidity into the banking system, the central bank stated that it would spend D20.3trn (US\$1.2bn) to pay off the compulsory bonds that it had forced banks to buy in March, although it is not compulsory for banks to sell them at any given time. It also lowered the required reserve ratio on dong deposits to 10% and that on US dollar deposits to 9%; both rates had previously been set at 11%. In addition, the SBV doubled the interest rate that it pays on required commercial bank reserves to 10%.

The net effect was that by early November banks were awash with funds. The base interest rate cuts have allowed banks to lower their lending rates, which were as high as 21% earlier this year. (The SBV caps the lending rate at 1.5 times the base rate, and until recently many banks were charging exactly that in order to attract deposits.) However, in the current environment it may take some time for banks to find good-quality borrowers. The SBV has urged banks to focus on the quality of credit, especially for real estate loans (which account for around 9% of all outstanding loans), and to expand lending to encourage exports, farming and large national projects.

The currency trading band is widened to 3%

The SBV has widened the trading band within which the dong can fluctuate against the US dollar on a daily basis to 3%, from 2% previously. The global financial crisis and recessionary conditions in the US, Vietnam's largest export market, have dampened the prospects for buoyant economic growth in 2009. The move is intended to allow a quicker, albeit heavily managed, depreciation of the dong against the US dollar, making Vietnamese exports cheaper and encouraging export growth. However, import demand in the US and the EU is forecast to contract in 2009, creating a dreary outlook for Vietnam's export sector, regardless of how cheap exports may become.

Despite some bad debts, banks are solvent

According to the deputy governor of the SBV, Nguyen Dong Tien, bad loans held by commercial banks totalled D35trn on September 30th, equivalent to 2.9% of all outstanding loans. (Figures from the SBV differ from those used by the Economist Intelligence Unit, owing to our doubts about the accuracy of national data on the banking sector.) The SBV expects the figure to rise to no more than 4% by the end of the year, which should still be manageable given that all credit institutions have capital adequacy ratios above the minimum of 8%. Nonetheless, the SBV is insisting that by the end of 2008 every bank should have chartered capital of at least D1trn. This poses a dilemma for the nine joint-stock banks whose capital is below this level. These banks will either have to raise more capital or merge. The former approach is likely to prove difficult considering that the stockmarket is still performing dismally and deposit interest rates are decreasing.

The government wants to raise electricity prices

Serious disagreement has broken out about the appropriate level at which to set electricity prices. The government has said that it plans gradually to remove subsidies on the electricity that it provides to the state-owned Electricity of Vietnam (EVN, the country's power supplier) beginning in 2009, as a prelude to greater liberalisation. The current retail price averages D862/kwh (5 US cents/kwh), and the Ministry of Trade is considering raising prices by up to 20% in 2009. Some members of the National Assembly are unhappy about the proposal, highlighting EVN's significant after-tax profits in recent years. EVN did not help its cause by asking the government in mid-October this year to allow it to use D1trn that it had received from price increases in 2007 to reward its staff.

The problem is that while the average cost to consumers of electricity generated by EVN is relatively low, this is largely a legacy effect. The country's largest hydroelectric plant, the Hoa Binh facility, is inexpensive to run, and the capital costs have never been fully passed on to consumers. EVN now says that it needs more than US\$2.5bn annually to invest in power plants, but it cannot raise enough money unless the price of electricity is high enough to reassure lenders of its capacity to service its loans. In late October the SBV essentially ordered the large state-owned commercial banks to lend to EVN for "important power generation projects", an echo of a time when most lending was directed by the authorities.

The minimum wage will rise on January 1st 2009

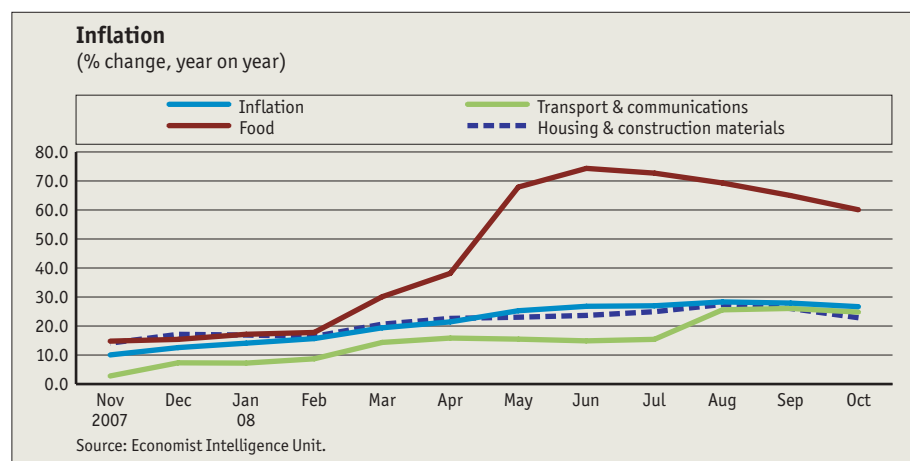
The government has approved an increase of around 20% in the minimum wage from January 1st 2009. This will help to maintain calm in the labour market and boost private consumption. The new minimum wage will vary by

location and by the ownership status of the firm concerned: foreign-invested firms will pay a minimum of D1.2m (US\$75) per month in the major cities and D920,000 (US\$58) in rural areas, while domestic firms will have to pay at least D800,000 in large cities and D690,000 in rural areas. Inflation, which is estimated at around 25% year on year in 2008, has eroded real wages. Consequently, households will feel scarcely any benefit from the wage increases.

Economic performance

Consumer prices fall by 0.2% month on month in October

Consumer prices fell by 0.2% month on month in October, signalling a clear end, at least in the short term, to the increase in inflation that characterised the first three quarters of 2008. After declining in every month since July, food prices fell again, by 1.9% month on month, in October, while prices for food and foodstuffs fell by 0.5% in that month. Considering that food and foodstuffs account for around 43% of the basket of goods and services that is used to calculate the consumer price index, this is an indication that domestic prices are beginning to fall. Moreover, both housing and construction costs and transport and communications prices dropped in month-on-month terms in October. These reductions reflected the lower prices of commodities and raw materials, including rice, steel and petroleum. Despite the recent fall in prices, inflation reached 26.7% year on year in October, but this is mostly a reflection of the rapid rise in prices earlier in 2008.



Despite the fall in consumer prices, inflation could be pushed up again by rising bank credit and the depreciation of the dong against the US dollar. The SBV's moves to increase liquidity in the domestic market may boost inflationary pressures. Moreover, the depreciation of the local currency against the US dollar will make imports more expensive, which could also exert upward pressure on inflation. Despite the risks, the SBV is hoping that overall inflation will continue to fall, as the slowdown in the domestic economy and the ensuing decrease in domestic demand (which boosted inflationary pressures in 2008) will outweigh the inflationary impact of a weaker currency and increased liquidity.

Commodity prices are declining quickly

Although the slowdown in domestic economic growth has been modest so far, Vietnam will not escape unscathed from the global financial crisis. Export-oriented firms are particularly concerned about the poor outlook for growth in the country's major export markets, including the US, the EU and Japan. Moreover, the challenge of adapting to declining commodity prices is now being faced by companies throughout the Vietnamese economy.

It appears that July represented a cyclical peak in steel prices, as prices have since given up the bulk of the gains that they made in January-July. The extremely high prices encouraged a significant rise in global supply, which largely went into inventory. As underlying demand slowed, buyers did not need to secure any more steel, and the lack of buying activity was compounded by the progressive reduction in credit availability to international traders and consumers. Much of the steel that was purchased at high prices in Vietnam by distributors earlier in the year is now sitting unsold. Local firms reportedly now have stocks amounting to 900,000 tonnes (with a value of close to US\$1bn), which remain unsold. Moreover, buyers expect further price reductions, and so are postponing purchases. Local steel companies are therefore facing both the high costs of holding stocks and also low prices.

The price of rice, meanwhile, almost tripled in the first five months of 2008, but has since fallen by around one-third. Some farmers are angry that they were not allowed to export more rice when world prices were high, as the government was concerned about domestic food price inflation and the possibility of shortages. Rice exporters are now reluctant to buy from farmers until they have firm export contracts, in case they are left holding stockpiles. The relatively high cost of credit has also deterred such purchases.

Exports are falling in US dollar terms

Since June the monthly trade deficit has narrowed drastically, supporting the balance-of-payments position, but both exports and imports have been on a falling trend since July. In monthly terms the trade deficit narrowed to US\$700m in October, from a high of US\$2.9bn in May, as a result of slower import growth. In the first ten months of 2008 Vietnam exported US\$52.1bn-worth of goods, an increase of 32% compared with the year-earlier period. Imports rose by 45% in January-October to reach US\$67.5bn, leaving a trade deficit of US\$15.4bn—more than one-and-a-half times the deficit recorded for the whole of 2007. These figures mask a dramatic slowdown in the value of trade. Exports have been moving downwards steadily since July, while imports have followed the same trend since May, albeit falling by a greater amount. Much of the decrease in the value of imports is a result of falling global prices for commodities, such as steel, as well as decreased demand for vehicles. Vietnam will face a difficult trade environment in 2009, especially as demand from its major export markets contracts.

PetroVietnam wants a foreign partner for an oil refinery

As local production of crude oil continues to decline, state-owned PetroVietnam is negotiating with international suppliers, including UK-based BP and Royal Dutch/Shell, an Anglo-Dutch firm, to provide oil for a new refinery in Dung Quat. The refinery, which when at full capacity will have a throughput of 140,000 barrels/day, is due to begin operations in February 2009, and will

initially receive almost one-third of its crude oil from overseas. PetroVietnam has asked for government permission to sell part of the refinery to foreign investors, who have so far shunned the Dung Quat project owing to its impractical location and soaring costs, making the likelihood of such a deal uncertain at present. The government has noted that the country's oil is of relatively high quality, making it more profitable to export some of it to refineries elsewhere and to import lower-quality oil for the new refinery. Moreover, as the Bach Ho field, which is the refinery's primary supplier, has already passed its peak level of production, it seems likely that PetroVietnam is trying to line up a strategic partner that would ensure supplies of crude oil to the refinery well into the future. At the outset the refinery will require 3.5m tonnes of crude oil annually, rising to 6.5m tonnes in 2010. Vietnam produced 15.5m tonnes of crude in 2007.

Data and charts

Annual data and forecast

	2004 ^a	2005 ^a	2006 ^a	2007 ^a	2008 ^b	2009 ^c	2010 ^c
GDP							
Nominal GDP (US\$ bn)	45.4	52.9	60.9	71.1	84.7	94.4	105.9
Nominal GDP (D bn)	715,307	839,211	974,266	1,144,020	1,401,585	1,604,888	1,810,493
Real GDP growth (%)	7.8	8.4	8.2	8.5	6.1	4.3	5.3
Expenditure on GDP (% real change)							
Private consumption	7.1	7.3	8.3	9.6 ^b	3.9	2.8	3.3
Government consumption	7.8	7.9	8.8	8.9 ^b	5.2	5.0	5.5
Gross fixed investment	10.4	9.8	9.9	23.0 ^b	15.0	7.8	8.0
Exports of goods & services	25.7	20.5	17.2 ^b	15.2 ^b	10.5	1.9	3.6
Imports of goods & services	21.9	15.9	15.6 ^b	21.3 ^b	15.2	1.4	3.0
Origin of GDP (% real change)							
Agriculture	4.4	4.0	3.4	3.4	3.5	3.0	2.0
Industry	10.3	10.7	10.4	10.6	8.2	6.5	6.8
Services	7.3	8.5	8.3	8.7	5.1	2.6	5.1
Population and income							
Population (m)	82.7	83.5	84.4 ^b	85.3 ^b	86.1	87.0	87.8
GDP per head (US\$ at PPP)	1,932 ^b	2,132 ^b	2,357 ^b	2,599 ^b	2,830	2,977	3,142
Recorded unemployment (av; %)	5.6	5.3	4.8	4.6 ^b	4.9	5.2	5.5
Fiscal indicators (% of GDP)							
Central government balance	-3.3	-4.1	-2.9	-5.4 ^b	-4.7	-6.8	-6.6
Net public debt	42.7	44.0	45.9 ^b	48.1 ^b	46.7	50.1	53.3
Prices and financial indicators							
Exchange rate D:US\$ (end-period)	15,777	15,916	16,054	16,030	17,200	17,163	16,930
Exchange rate D:€ (end-period)	21,359	18,775	21,186	23,409	22,016	22,312	22,094
Consumer prices (end-period; %)	9.7	8.6	6.6	14.4	20.9	5.1	8.4
Stock of money M1 (% change)	26.1	22.2	20.7	48.9	-1.6	-4.2	-0.6
Stock of money M2 (% change)	31.1	30.9	29.7	49.1	13.0	-1.3	13.3
Lending interest rate (av; %)	9.7	11.0	11.2	11.2	16.1	12.6	10.1
Current account (US\$ m)							
Trade balance	-2,287	-2,439	-2,776	-10,360	-14,612	-8,762	-6,373
Goods: exports fob	26,485	32,447	39,826	48,561	61,975	49,255	55,185
Goods: imports fob	-28,772	-34,887	-42,602	-58,921	-76,586	-58,016	-61,558
Services balance	-872	-296	-8	-894	-1,163	-823	-954
Income balance	-891	-1,205	-1,429	-2,168	-1,778	-1,236	-1,246
Current transfers balance	3,093	3,380	4,049	6,430	5,968	5,235	5,502
Current-account balance	-957	-560	-164	-6,993	-11,585	-5,586	-3,071
External debt (US\$ m)							
Debt stock	18,049	19,212	20,202	21,848 ^b	23,194	22,319	23,052
Debt service paid	787	957	918	944 ^b	1,029	1,034	1,070
Principal repayments	430	519	464	533 ^b	570	666	672
Interest	357	438	454	411 ^b	459	368	397
International reserves (US\$ m)							
Total international reserves	7,186	9,217	13,591	23,872	21,803	19,586	22,170

^a Actual. ^b Economist Intelligence Unit estimates. ^c Economist Intelligence Unit forecasts.

Source: IMF, *International Financial Statistics*.

Quarterly data

	2006	2007				2008		
	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr
Prices								
Consumer prices (2000=100)	136.0	140.1	142.7	146.8	152.9	165.7	177.5	189.4
Consumer prices (% change, year on year)	6.7	6.5	7.4	9.1	12.4	18.3	24.4	29.0
Financial indicators								
Exchange rate D:US\$ (av)	16,077	16,022	16,070	16,206	16,084	15,947	16,252	16,666
Exchange rate D:US\$ (end-period)	16,054	16,024	16,125	16,105	16,030	15,898	16,490	16,596
Deposit rate (av; %)	7.7	7.7	7.6	7.4	7.3	9.1	13.8	n/a
Lending rate (av; %)	11.2	11.2	11.2	11.2	11.2	12.3	16.6	n/a
Refinancing rate (end-period; %)	6.5	6.5	6.5	6.5	6.5	7.5	15.0	n/a
Treasury bill rate (av; %)	3.4	3.6	4.1	4.8	n/a	n/a	n/a	n/a
M1 (end-period; D trn)	292.2	317.3	334.4	352.8	435.2	396.1	342.1	n/a
M1 (% change, year on year)	20.7	31.3	40.4	49.2	48.9	24.8	2.3	n/a
M2 (end-period; D trn)	841.0	949.2	1,029.6	1,111.0	1,254.0	1,300.2	1,295.5	n/a
M2 (% change, year on year)	29.7	35.6	41.6	47.5	49.1	37.0	25.8	n/a
Foreign trade (US\$ m)								
Exports fob	10,133	10,565	11,901	12,319	13,528	13,160	15,750	n/a
Imports cif	-11,591	-12,277	-14,783	-15,537	-18,100	-21,510	-22,650	n/a
Trade balance	-1,458	-1,712	-2,882	-3,218	-4,572	-8,350	-6,900	n/a
Foreign payments (US\$ m)								
Merchandise trade balance	-1073.0	-974.0	-2047.0	-2298.0	-5041.0	n/a	n/a	n/a
Services balance	51	-142	-284	-209	-259	n/a	n/a	n/a
Income balance	-301	-400	-803	-387	-578	n/a	n/a	n/a
Net transfer payments	1,572	1,564	1,774	1,473	1,619	n/a	n/a	n/a
Current-account balance	249	47	-1,360	-1,421	-4,259	n/a	n/a	n/a
Reserves excl gold (end-period)	13,384	18,317	20,793	22,575	23,602	25,049	20,979	n/a

Sources: IMF, *International Financial Statistics*.

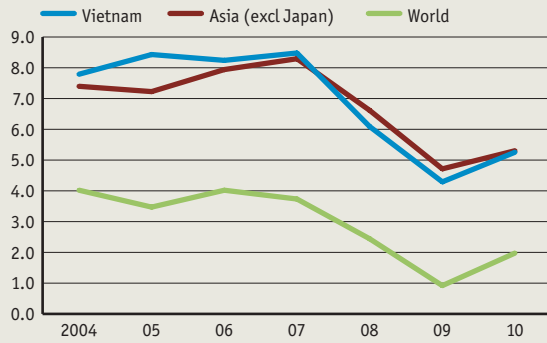
Monthly data

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Exchange rate D:US\$ (av)												
2006	15,924	15,924	15,914	15,930	15,973	15,989	15,997	16,011	16,038	16,065	16,093	16,073
2007	16,061	15,994	16,012	16,039	16,062	16,109	16,139	16,240	16,239	16,109	16,093	16,051
2008	16,016	15,940	15,731	16,126	16,171	16,490	16,798	16,605	16,596	n/a	n/a	n/a
Exchange rate D:US\$ (end-period)												
2006	15,922	15,910	15,927	15,934	15,959	15,996	16,007	16,014	16,055	16,083	16,089	16,054
2007	16,036	15,990	16,024	16,047	16,087	16,125	16,147	16,270	16,105	16,100	16,070	16,030
2008	16,005	15,750	16,125	16,175	16,246	16,842	n/a	n/a	n/a	n/a	n/a	n/a
Money supply M1 (% change, year on year)												
2006	29.8	18.2	24.4	21.5	23.1	22.0	23.9	22.7	17.6	18.7	20.5	20.7
2007	16.2	35.4	31.3	35.7	37.4	40.4	43.1	41.9	49.2	55.4	53.7	48.9
2008	56.8	35.3	24.8	17.7	10.9	2.3	n/a	n/a	n/a	n/a	n/a	n/a
Money supply M2 (% change, year on year)												
2006	34.6	32.5	35.4	33.8	34.1	33.5	34.1	32.7	30.3	30.4	30.6	29.7
2007	28.8	34.0	35.6	39.0	40.6	41.6	43.7	43.2	47.5	50.5	49.8	49.1
2008	48.2	41.4	37.0	30.5	29.1	25.8	n/a	n/a	n/a	n/a	n/a	n/a
Deposit rate (av; %)												
2006	7.5	7.7	7.7	7.7	7.5	7.7	7.7	7.7	7.7	7.7	7.7	7.7
2007	7.7	7.7	7.7	7.7	7.7	7.4	7.4	7.4	7.4	7.4	7.2	7.2
2008	7.2	9.0	11.2	11.5	13.3	16.6	n/a	n/a	n/a	n/a	n/a	n/a
Lending rate (av; %)												
2006	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
2007	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
2008	11.2	11.2	14.6	14.3	16.5	19.1	n/a	n/a	n/a	n/a	n/a	n/a
Consumer prices (av; % change, year on year)												
2006	8.8	8.3	7.8	7.2	7.4	7.4	7.4	7.3	6.8	6.7	6.8	6.6
2007	6.5	6.5	6.7	7.1	7.2	7.8	8.4	8.6	10.5	11.0	11.8	14.4
2008	15.9	17.5	21.4	23.3	27.2	28.8	29.1	28.3	27.9	n/a	n/a	n/a
Goods exports fob (US\$ m)												
2006	3,065	2,404	3,100	3,200	3,200	3,400	3,500	3,674	3,378	3,343	3,290	3,500
2007	3,759	2,925	3,881	3,650	4,066	4,185	4,278	4,313	3,728	4,280	4,548	4,700
2008	4,911	3,415	4,834	5,088	5,150	5,500	6,547	6,100	n/a	n/a	n/a	n/a
Goods imports cif (US\$ m)												
2006	2,599	2,714	3,200	3,500	3,600	4,000	4,050	4,151	3,968	3,845	3,746	4,000
2007	4,331	3,468	4,478	4,493	5,279	5,011	5,239	5,335	4,963	5,630	6,170	6,300
2008	7,198	6,194	8,118	8,307	8,000	6,800	7,300	7,000	n/a	n/a	n/a	n/a
Trade balance fob-cif (US\$ m)												
2006	466	-310	-100	-300	-400	-600	-550	-477	-590	-502	-456	-500
2007	-572	-543	-597	-843	-1,213	-826	-961	-1,022	-1,235	-1,350	-1,622	-1,600
2008	-2,287	-2,779	-3,284	-3,219	-2,850	-1,300	-753	-900	n/a	n/a	n/a	n/a
Foreign-exchange reserves excl gold (US\$ m)												
2006	9,993	10,199	10,742	11,180	11,391	11,293	11,357	11,684	11,904	12,015	12,291	13,384
2007	15,265	16,967	18,317	19,300	20,267	20,793	21,701	21,925	22,575	23,036	23,509	23,602
2008	24,467	26,328	25,049	23,464	22,175	20,979	n/a	n/a	n/a	n/a	n/a	n/a

Sources: IMF, *International Financial Statistics*; Haver Analytics.

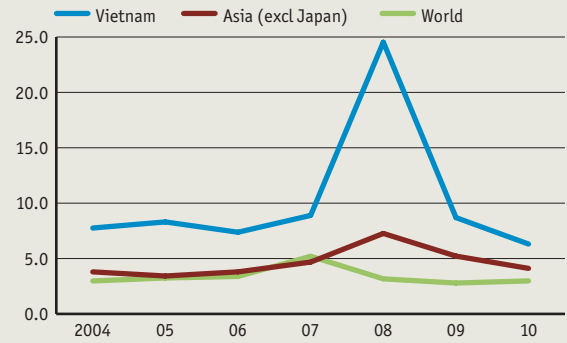
Annual trends charts

Real GDP growth
(% change)



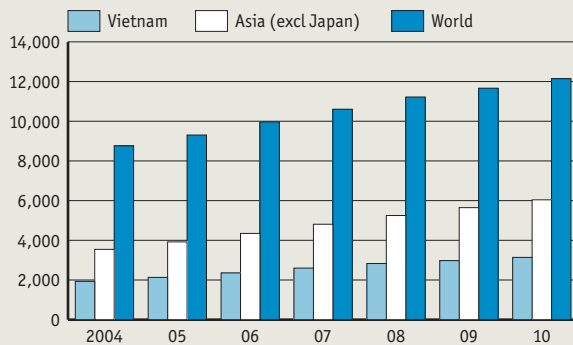
Source: Economist Intelligence Unit.

Consumer price inflation
(% change, year on year; av)



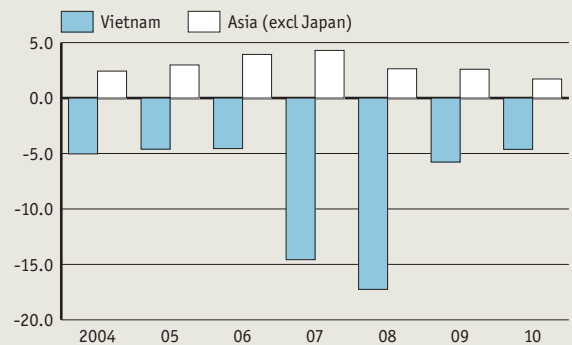
Source: Economist Intelligence Unit.

GDP per head
(US\$, PPP)



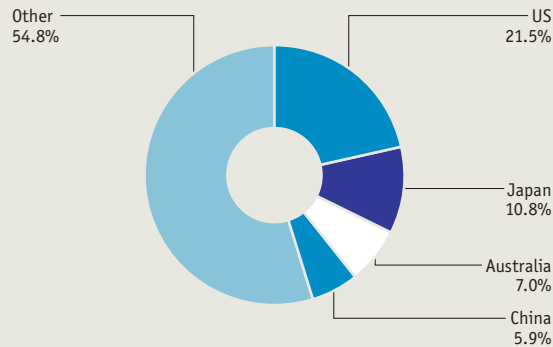
Source: Economist Intelligence Unit.

Trade balance
(% of GDP)



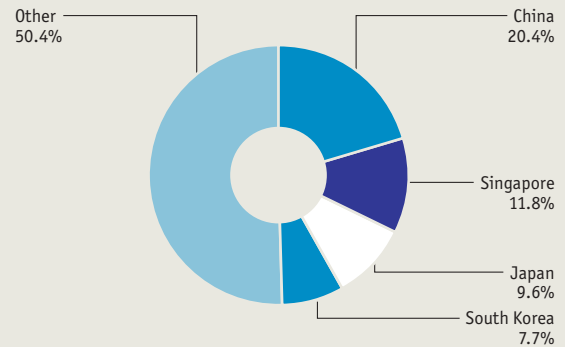
Source: Economist Intelligence Unit.

Main origins of exports, 2007
(share of total)



Source: Economist Intelligence Unit.

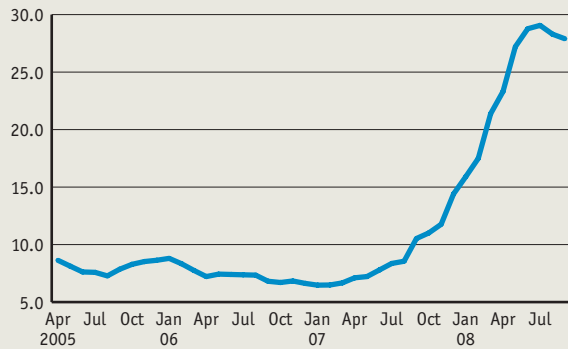
Main origins of imports, 2007
(share of total)



Source: Economist Intelligence Unit.

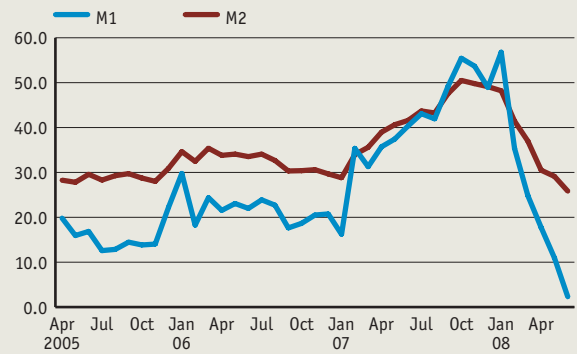
Monthly trends charts

Consumer price inflation
(% change, year on year)



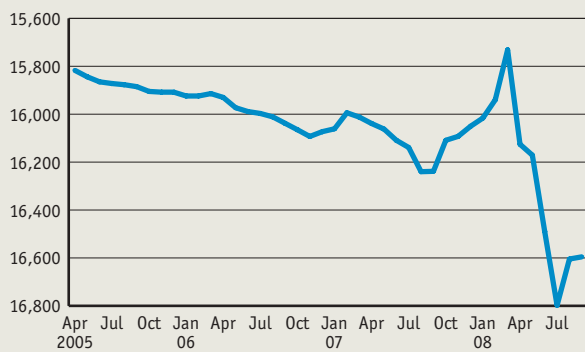
Source: Economist Intelligence Unit.

Monetary aggregates
(% change, year on year)



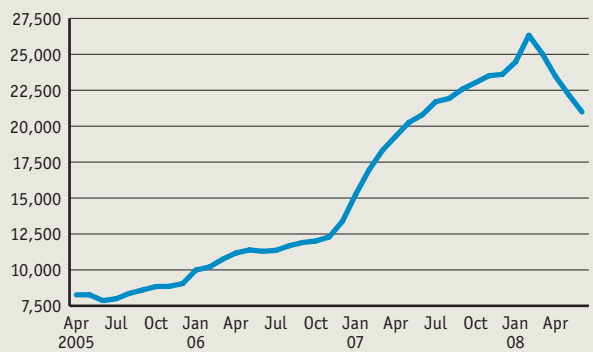
Source: Economist Intelligence Unit.

Exchange rate
(D:US\$; av; inverted scale)



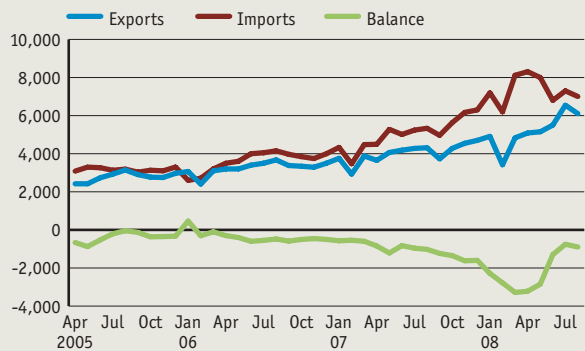
Source: Economist Intelligence Unit.

Foreign-exchange reserves
(US\$ m)



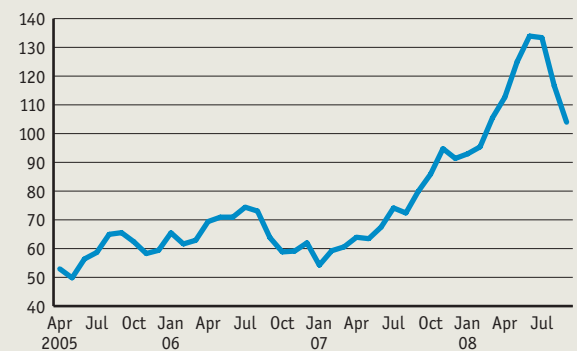
Source: Economist Intelligence Unit.

Foreign trade
(US\$ m; goods only)



Source: Economist Intelligence Unit.

Oil: WTI crude price
(US\$/b; av)



Source: Economist Intelligence Unit.

Country snapshot

Political structure

Official name	Socialist Republic of Vietnam	
Form of state	One-party rule	
The executive	The cabinet is constitutionally responsible to the National Assembly, which is elected for a five-year term	
Head of state	The president, currently Nguyen Minh Triet	
National legislature	The unicameral 493-member Quoc Hoi (National Assembly) meets biannually; an election takes place every five years. The Assembly appoints the president and the cabinet	
Local government	Centrally controlled provinces and municipalities are subdivided into towns, districts and villages, which have a degree of local accountability through elected people's councils	
Legal system	The regional people's courts and military courts operate as courts of first and second instance, with the Supreme Court at the apex of the system	
National elections	Elections for the National Assembly and People's Councils took place in May 2007; the next are due in 2012	
National government	The Communist Party of Vietnam, and in particular its politburo, controls both the electoral process and the executive	
Main political organisations	The Communist Party of Vietnam (general secretary: Nong Duc Manh); the Vietnam Fatherland Front	
Main members of the cabinet	Prime minister	Nguyen Tan Dung
	Deputy prime ministers	Nguyen Sinh Hung Pham Gia Khiem Hoang Trung Hai Nguyen Thien Nhan Truong Vinh Trong
	Key ministers	Agriculture & rural development Cao Duc Phat Construction Nguyen Hong Quan Culture, sports & tourism Hoang Tuan Anh Education & training Nguyen Thien Nhan Finance Vu Van Ninh Foreign affairs Pham Gia Khiem Industry & trade Vu Huy Hoang Information & communications Le Doan Hop Interior Tran Van Tuan Justice Ha Hung Cuong Labour, war invalids & social affairs Nguyen Thi Kim Ngan National defence Phung Quang Thanh Natural resources & environment Pham Khoi Nguyen Planning & investment Vo Hong Phuc Public health Nguyen Quoc Trieu Transport Ho Nghia Dung
Central bank governor	Nguyen Van Giau	